<u>ESA consultation – comments by Ministry of Finance NL</u>

Question 1. Do you have any general comments on the draft Guidelines on the prudential assessment of acquisitions and increases of qualifying holdings in the financial sector?

Introduction

- Thank you for the possibility to comment on the draft Guidelines on the prudential assessment of acquisitions and increases of qualifying holdings in the financial sector. We would like to use this opportunity to draw your attention to an omission we see in the Qualifying Holdings Directive (QHD).[1] The issue is related to the risks to financial stability and resolvability that may stem from the merger or acquisition of a financial institution.
- The financial crisis has demonstrated that mergers and acquisitions – at least in the banking sector – can lead to financial stability risks. Currently, financial stability is only implicitly addressed by the current assessment criteria of the QHD. This issue was also mentioned in the report from the European Commission in February 2013.[2] In this report the Commission stated that currently the Directive does not contain an explicit assessment criterion allowing competent authorities to assess the impact of the proposed acquisition on the stability of the financial system. Therefore, the Commission suggested that – in light of the financial crisis – it might be considered to incorporate financial stability aspects more explicitly in the assessment process. The Commission intended to carry out an analysis in the course of 2013 assessing different options, which until now has not been finalised yet.
- The Netherlands suggests to include extra criteria on financial stability and resolvability in the list of criteria on which competent authorities have to evaluate mergers and acquisitions. Such criteria should be designated in a way that avoids divergent implementation by competent authorities. Below, the Netherlands presents the arguments for and different options to introduce a financial stability and resolvability assessment in the QHD.

Reason for the proposal

New financial regulation in the form of CRDIV as well as the introduction of the Single Supervisory Mechanism (SSM) and Single Resolution Mechanism (SRM) in the Eurozone brings us closer to a single market for banking services in the European Union, making (cross-border) consolidation more appealing. While a more perfect internal market can be beneficial for institutions and the financial system as a whole through diversification and economies of scale, consolidation could also create new potential too-big-to-fail problems. This is to be prevented as mergers and acquisitions typically make banks substantially larger, less substitutable, more complex and more interconnected with other parts of the financial system.

At the moment the evaluation criteria in the QHD are all micro-prudential in nature:

1. the reputation of the proposed acquirer;
2. the reputation and experience of any person who will direct the business of the credit institution as a result of the proposed acquisition;
3. the financial soundness of the proposed acquirer;
4. compliance with the prudential requirements of the target undertaking;
5. suspicion of money laundering or terrorist financing by the proposed acquirer.

These criteria as such do not take into account wider systemic implications or the resolvability of an institution resulting from a merger or acquisition. In other words, the QHD currently does not explicitly provide a legal ground to attach conditions to or refuse an acquisition on the basis of a risk to financial stability or resolvability.

Ensuring that competent and resolution authorities can assess the effects of an acquisition on financial stability and resolvability *before* the new entity is created, would help to prevent potential

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[1] DIRECTIVE 2007/44/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 5 September 2007 amending Council Directive 92/49/EEC and Directives 2002/83/EC, 2004/39/EC, 2005/68/EC and 2006/48/EC as regards procedural rules and evaluation criteria for the prudential assessment of acquisitions and increase of holdings in the financial sector.

[2] REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT, THE COUNCIL, THE EUROPEAN ECONOMIC AND SOCIAL COMMITTEE AND THE COMMITTEE OF THE REGIONS, Application of Directive 2007/44/EC amending Council Directive 92/49/EEC and Directives 2002/83/EC, 2004/39/EC, 2005/68/EC and 2006/48/EC as regards procedural rules and evaluation criteria for the prudential assessment of acquisitions.

too-big-to-fail institutions. This would, furthermore, prevent resolvability measures taken *ex post* by the resolution authorities reversing the acquisition immediately after it has taken place. Acting ex ante would thus safeguard financial stability as well as create more legal certainty for institutions. It is as such an important complementary measure to other recent regulatory initiatives.

Therefore, the Netherlands advocates the introduction of a financial stability and resolvability assessment in the QHD. Below we provide a few options how these criteria could be incorporated.

Options for Design

<u>Financial stability assessment</u>

- Under the SSM **the European Central Bank** (ECB) has the exclusive competence for both Significant Institutions (SIs) and Less Significant Institutions (LSIs) to assess notifications of proposed acquisitions. In non-SSM jurisdictions the **national competent authority** (NCA) has the power to review notifications of proposed acquisitions.
- The ECB or national competent authority should consider the following criteria in assessing the financial stability consequences of the proposed merger or acquisition: the size, complexity, interconnectedness and substitutability of the newly envisioned entity. These criteria are based on the **Basel and European standards** for identifying systemically important banks;
- To give guidance to the competent authority as to the application of these standards, certain **trigger values** could be introduced. These trigger values could be developed by EBA in coordination with the ECB and other national competent authorities. These triggers could be used to indicate when the competent authority should consider a case in more detail, and/or require prior conditions to the proposed merger or acquisition.
- In order to add an extra criterion on financial stability with respect to the prudential assessment of acquisitions and increases of qualifying holdings, two options could be considered:
    1. The financial stability criterion could be **explicitly incorporated** in one of the existing assessment criteria, e.g. the criteria on financial soundness of the proposed acquirer and on compliance with prudential requirements;
    2. Another solution could be to **add an extra criterion** to the list of the assessment criteria: for example "<u>impact of the proposed acquisition or increase of qualifying holding on the financial stability</u>".

Besides the need for an explicit (extra) criterion on financial stability, the Netherlands also stresses the importance to introduce a resolvability assessment in the QHD for reasons already mentioned above. The resolvability assessment could be designated in the following way.

<u>Resolvability assessment</u>

- The **Single Resolution Board** (SRB) or National Resolution Authority (NRA) is exclusively competent to judge whether an institution participating in the SSM is resolvable and to take measures to remove impediments to resolvability.
- The SRB/NRA, either independently or as part of the procedure by the ECB/NCA, should determine whether the future entity will be resolvable on the basis of **the criteria for resolvability** as defined in the SRM Regulation (art. 10) and the BRRD (art. 15-16).
- The resolvability assessment should be **added as an extra criterion** to the list of the assessment criteria: for example "<u>resolvability of the proposed acquisition or increase of qualifying holding</u>".